

109 FERC ¶ 61,204
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeene G. Kelly.

Northeast Utilities Service Company
and Select Energy, Inc.

Docket No. EL03-216-001

v.

ISO New England Inc. and
New England Power Pool

ORDER DENYING REHEARING

(Issued November 22, 2004)

1. In this order, the Commission denies the requests for rehearing of the Commission's order issued on October 24, 2003.¹ The October 24 Order, among other things, denied Northeast Utilities Service Company's (NUSCO)² and Select Energy, Inc.'s (Select Energy)³ (collectively, Northeast Utilities⁴) complaint against ISO New England (ISO-NE) and New England Power Pool (NEPOOL) regarding the calculation, collection and distribution of the loss component of the locational marginal prices (LMP) under New England's standard market design (NE-SMD). This order benefits customers in the Northeast by maintaining the NE-SMD LMP objectives.

¹ *Northeast Utilities Services Co.*, 105 FERC ¶ 61,122 (2003) (October 24 Order).

² NUSCO is a registered holding company and a service company subsidiary of Northeast Utilities.

³ Select Energy is a wholly-owned subsidiary of NU Enterprises, Inc., which is a wholly-owned subsidiary of Northeast Utilities.

⁴ Northeast Utilities filed on behalf of the Northeast Utilities Operating Companies, which are the Connecticut Light and Power Company, Western Massachusetts Electric Company, and the Public Service Company of New Hampshire.

Background

2. On July 15, 2002, NEPOOL and ISO-NE jointly filed a proposed standard market design for ISO-NE that included a congestion management system based on locational marginal pricing (LMP) and a multi-settlement system. The NE-SMD calculates the cost of transmission losses on a marginal cost basis to be collected as a component of LMP. In an order dated September 20, 2002,⁵ the Commission accepted the NE-SMD filing with certain modifications. The NE-SMD was implemented on March 1, 2003.

3. On July 23, 2003, Northeast Utilities filed a complaint against ISO-NE and NEPOOL. The complaint alleged that ISO-NE not only failed to file the formula and methodology for calculating transmission losses with the Commission, but the formula was “seriously flawed” since it resulted in “over-recovering physically-based transmission loss costs by many millions of dollars a month.”⁶ Specifically, Northeast Utilities asserted that the use of marginal losses in place of average losses in the calculation of LMPs had resulted in the collection of more revenues than were required to be paid to generators producing energy. Since excess loss revenues were refunded to participants based on their net real-time adjusted load obligations over all locations, Northeast Utilities argued that the reimbursement methodology resulted in some participants receiving a windfall, while others paid too much.⁷

4. In the October 24 Order, the Commission denied Northeast Utilities’ complaint. The Commission found that Northeast Utilities had not shown that the inclusion of marginal losses in LMP or the refund mechanism for over-recovered losses was no longer just and reasonable. The Commission explained that the marginal losses and refund mechanism at issue were a part of the SMD proposal NEPOOL and ISO-NE submitted to the Commission on July 15, 2002 and which the Commission accepted in the September 20 Order. The Commission emphasized that, notwithstanding the argument of Northeast Utilities, marginal losses typically are in excess of average losses, and this fact was widely known when the Commission accepted their inclusion in LMP rates.⁸ The Commission further emphasized that while the marginal loss costs may be greater than Northeast Utilities expected, that is not a basis to reject a methodology that the Commission previously accepted and is on file with the Commission.⁹

⁵ *New England Power Pool*, 100 FERC ¶ 61,287 (2002), *as amended* October 7, 2002 (September 20 Order).

⁶ Complaint at 3.

⁷ *Id.* at 15-16.

⁸ October 24 Order, 105 FERC ¶ 61,122 at P 19.

⁹ *Id.*

Request for Rehearing

5. Connecticut Department of Public Utility Control (CT DPUC), FPL Energy, LLC (FPL Energy) and Northeast Utilities filed requests for rehearing of the October 24 Order.

6. CT DPUC states that it is not arguing against the Commission's determination that the marginal loss mechanism was properly filed pursuant to section 205 or that the calculation of loss charges was appropriate. Rather, it explains that the purpose of its request is to recommend that the Commission modify the refund mechanism so that system costs and risks are reduced, and so that proper market incentives are created. CT DPUC contends that the current refund mechanism in the NE-SMD is arbitrary and capricious, and provides potentially tens of millions of dollars in windfall payments annually to participants who provide no products or services in return to the ratepayers who pay the line loss charges. Accordingly, it believes that the excess charges addressed by the refund mechanism are unjust and unreasonable. CT DPUC requests that the Commission clarify that ISO-NE, after conducting a stakeholder process, must file a new refund mechanism that "eliminates windfall payments to participants who are not providing products or services to the customers that pay the excess revenues and that uses the excess revenue to provide some benefits to customers who overpay or to pay for system costs actually incurred." In this regard, it recommends several options for using the excess revenues in an appropriate manner.

7. Northeast Utilities asks the Commission to clarify that the October 24 Order is not a decision on the merits as to the justness and reasonableness of the current marginal loss refund methodology. Northeast Utilities contends that while the Commission stated that the current loss refund methodology was filed as part of the Commission-accepted LMP calculations, this refund methodology has not been subject to direct Commission scrutiny and, accordingly, it has not been shown to be just and reasonable. According to Northeast Utilities, the current disbursement method arbitrarily provides some participants with a windfall. To equitably correct the excess loss collections, Northeast Utilities suggests that ISO-NE and NEPOOL consider adopting a new method to replace the "current, flawed disbursement scheme" and either: (1) use the excess loss collections to reduce the costs to participants of the ISO's operations, or (2) use the excess loss revenue surplus to reduce the Network Access Service charge – the charge used to recover the embedded costs of the transmission system.¹⁰ Either option, Northeast Utilities maintains, would allow the excess collections to benefit participants without

¹⁰ Northeast Utilities explains that the Commission proposed this alternative in its SMD Order (*see Remediating Undue Discrimination through Open Access Transmission Service and Standard Electricity Market Design, Notice of Proposed Rulemaking*, 67 Fed. Reg. 55,452 (Aug. 29, 2002), FERC Stats. & Regs. ¶ 32,563, Appendix B, §§ F.3.7.2 and F.4.5.1 (2002) (SMD NOPR)).

affecting locational prices or enriching only a few. Northeast Utilities requests that the Commission acknowledge that there are alternatives that could be developed through the NEPOOL stakeholder process.

8. FPL Energy argues that the Commission erred in not granting Northeast Utilities' complaint in the October 24 Order. First, it asserts that the Commission erred in not directing ISO-NE to file with the Commission how it calculates the penalty factor that it uses in calculating marginal losses; without this information, FPL Energy argues, LMP calculations cannot be replicated.

9. Next, it argues that ISO-NE's current method includes an error that results in unjust and unreasonable marginal loss calculations during times of congestion and transmission system constraints. FPL Energy, relying on the prepared direct testimony of Dr. Judith B. Cardell, which it is submitting for the first time in this proceeding, explains that when calculating marginal losses, ISO-NE uses a weighted average of the load buses throughout its system. ISO-NE, however, does not modify its practice when congestion exists, and in turn, FPL Energy explains, fails to adjust for the existence of transmission constraints in its marginal loss calculation, which likely overstates marginal losses. FPL Energy asserts that the Commission should direct ISO-NE to resettle LMPs during periods of congestion and refunds should be ordered from March 1, 2003, the date LMP was implemented in New England or, in the alternative, the effective date of the Northeast Utilities' complaint.

10. FPL Energy further argues that ISO-NE's current method of reallocating excess recovery of revenue associated with the use of marginal losses is unjust and unreasonable as it distorts price signals to load. By not disclosing exactly what method it uses to calculate the penalty factor, FPL Energy contends, the LMP method is not transparent, thereby undermining the value and degrades the intended economic signals sent to participants, i.e., the conveying of dispatch signals and investment or siting incentives. In particular, FPL Energy states, the long-run signal is intended to indicate where new generation and load should be sited, but this signal is distorted in the manner by which ISO-NE reallocates the over-collected losses to load. FPL Energy further states that the challenge is to develop a methodology for allocating the over-collection of loss revenues in a manner that does not distort the price signal that LMP is sending and is not subject to gaming. It asserts that, to date, each method that has been proposed has certain flaws. Stating that there is no "one accepted textbook method" for calculating and implementing marginal losses, FPL Energy includes a White Paper that proposes another option for allocating the over-collection of loss revenues.¹¹ FPL Energy explains that its proposed alternative is market-based and would allow generators and load to hedge their losses through the ability to self-supply.

¹¹ See FPL Energy, LLC Request for Rehearing, Exhibit FPL-3 (A Proposal for a Market-Based Mechanism for Allocation of the Surplus Revenues from the Calculation and Charging of Marginal Losses) (White Paper).

11. Finally, FPL Energy asserts that the Commission erred in basing the denial of Northeast Utilities' complaint on the fact that it had failed to point to anything in prior Commission proceedings indicating what marginal loss costs were expected.

Answers

12. On December 9, 2003, ISO-NE filed a response to FPL Energy's request for rehearing. In response, on January 6, 2004, FPL Energy filed an answer to ISO-NE's answer.

Discussion

A. Procedural Matters

13. Rule 713 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.713(d) (2004), prohibits answers to rehearing requests. Accordingly, we will reject ISO-NE's answer. Because we are rejecting ISO-NE's answer, we will also reject FPL Energy's answer.

B. Commission Conclusion

14. We will deny CT DPUC's rehearing request. CT DPUC contends that the current marginal cost refund mechanism is arbitrary and capricious, and asks the Commission to require the ISO-NE, after conducting a stakeholder process, to file a new refund mechanism that, according to CT DPUC, would result in the use of excess revenues in an appropriate manner. In the October 24 Order, the Commission found that the complainant, Northeast Utilities, failed to show that the inclusion of marginal losses in LMP or the refund mechanism for over-recovered losses is no longer just and reasonable as required by section 206 of the Federal Power Act, and accordingly rejected Northeast Utilities' complaint.¹² CT DPUC has provided no evidence that the Commission erred in making that determination. The fact that CT DPUC believes that there may be a better approach to the currently effective marginal cost refund mechanism does not render the current mechanism unjust and unreasonable. The Commission itself recognized in the October 24 Order that the refunding of excess loss revenues could be done in many ways, but emphasized that it should not be done in a manner that undermines the LMP calculation.¹³ Moreover, even if the Commission were to find the current methodology no longer just and reasonable, CT DPUC has failed to provide a just and reasonable

¹² October 24 Order, 105 FERC ¶ 61,122 at P 18-22.

¹³ *Id.* at P 20.

alternative methodology.¹⁴ Rather, CT DPUC merely suggests some possibilities and requests that the Commission require ISO-NE, after conducting a stakeholder process, to file a new refund mechanism. CT DPUC did not satisfy its obligation under section 206 of the FPA of demonstrating a new methodology that is just and reasonable.¹⁵ If CT DPUC desires to continue to pursue this issue, it should raise the issue with ISO-NE and seek to have its suggestions addressed through the ISO-NE's stakeholder process. Alternatively, CT DPUC could file its own complaint, with the reminder that it must meet the obligations of section 206 of demonstrating that the current methodology is unjust and unreasonable and that an alternative replacement methodology is just and reasonable.

15. We will deny Northeast Utilities' rehearing request that the Commission clarify that it has not specifically considered or specifically approved the current method for allocating excess loss collections. In the September 20 Order, the Commission accepted, without suspension or hearing, the NE-SMD, as modified, submitted jointly by NEPOOL and ISO-NE.¹⁶ The NE-SMD included a congestion management system based on LMP and a multi-settlement system. The NE-SMD also provided that the cost of transmission losses would be calculated on a marginal cost basis and collected as a component of LMP.¹⁷ The Commission accepted the filing, including the method for calculating losses on a marginal cost basis, without suspension or hearing. Thus, contrary to Northeast Utilities' assertions, the LMP methodology, including the method for calculating losses

¹⁴ See *Investigation of Terms and Conditions of Public Utility Market-Based Rate Authorizations*, 107 FERC ¶ 61,175 (2004) (the complainant has the burden of proof when challenging an existing rate as unjust and unreasonable); see also *Public Service Commission of the State of New York v. FERC*, 642 F.2d 1335 (D.C. Cir. 1980); *ANR Pipelines Co. v. FERC*, 771 F.2d 507 (D.C. Cir. 1985); *Southern LNG Inc.*, 90 FERC ¶ 61,257 (2000) (the complainant must demonstrate with substantial and specific evidence that the existing rates are unjust, unreasonable, unduly discriminatory or preferential and that its proposed rates are just and reasonable).

¹⁵ *Tesoro Alaska Petroleum Co. v. FERC*, 234 F.3d 1286 (2000) (the party seeking to change the current methodology bears the burden of proving that changed circumstances require the existing valuation be found to be unjust and unreasonable).

¹⁶ *New England Power Pool*, 100 FERC ¶ 61,287 at Ordering Paragraph A (2002). Further, in *New England Power Pool*, 102 FERC ¶ 61,248 (2003), the Commission permitted the tariff to go into effect on March 1, 2003.

¹⁷ See NE-SMD Application in Docket No. ER02-2330-000, Transmittal Letter at 15-16 (which explains that the marginal losses will be part of the LMP calculation and explains the methodology that will be used for the allocation of the marginal loss revenue); see also NEPOOL FERC Electric Rate Schedule No. 7, Market Rule 1, Original Sheet Nos. 44-49.

on a marginal cost basis, was found to be just and reasonable. Moreover, in the October 24 Order, the Commission specifically noted that the marginal losses and the refund mechanism were part of the Commission-accepted LMP calculations and are currently part of the rate on file with the Commission.¹⁸ In this regard, the Commission further noted that Northeast Utilities had not sought rehearing of the September 20 Order and that the arguments in its complaint concerning the methodologies for marginal losses and refunds were essentially a collateral attack on that order.¹⁹ Thus, contrary to Northeast Utilities' assertions, the current rate on file with the Commission, which includes the methodologies for marginal losses and refunds, was accepted by the Commission, without suspension or hearing, as just and reasonable.²⁰

16. We will deny FPL Energy's request for rehearing. FPL Energy raises a variety of new issues and provides extensive new evidence in the form of the prepared direct testimony of Dr. Judith B. Cardell and a White Paper. Much of what FPL Energy raises on rehearing goes well beyond the complaint filed in this proceeding and the Commission's order addressing that complaint, and is supported by evidence presented and arguments made for the first time in this proceeding. The Commission has repeatedly looked with disfavor on parties raising new issues and arguments for the first time on rehearing.²¹ In this regard, the Commission has explained that:

by raising its arguments for the first time on rehearing, [a party] has effectively precluded [other parties] from responding, as answers to requests for rehearing generally are prohibited under Rule 713(d)(1) of the Commission's Rules of Practice and Procedure. Moreover, . . . [w]e look with disfavor on parties raising

¹⁸ October 24 Order, 105 FERC ¶ 61,122 at P 18.

¹⁹ *Id.* at n. 44.

²⁰ We remind the parties that while they are free to propose alternatives to the filed rate and can pursue alternatives through the NEPOOL stakeholder process, because the current rate on file with the Commission has been found to be just and reasonable, a party proposing an alternative must demonstrate not only that its proposed methodology is just and reasonable, but also that the current methodology on file with the Commission is no longer just and reasonable.

²¹ See, e.g., *New York Independent System Operator, Inc.*, 95 FERC ¶ 61,347 (2001), citing *Baltimore Gas & Electric Company, et al.*, 91 FERC ¶ 61,270 at 61,922 (2000); see also *Philadelphia Electric Company*, 58 FERC ¶ 61,060 at 61,133 & n. 4 (1992).

on rehearing issues that should have been raised earlier. Such behavior is disruptive to the administrative process because it has the effect of moving the target for parties seeking a final administrative decision.^[22]

17. Further, with respect to FPL Energy's attempt to submit new evidence at this stage of the proceeding, the Commission has stated that it "generally will not consider new evidence on rehearing, because we cannot resolve issues with any efficiency or finality if parties are permitted to submit new evidence on rehearing and thus to have us chase a moving target."²³

18. Here, we reject FPL Energy's attempts to submit new issues and arguments, as well as new evidence, at the rehearing stage of this proceeding. In particular, FPL Energy asserts that ISO-NE's current method includes an error that results in unjust and unreasonable marginal loss calculations during times of congestion and transmission system constraints. This argument was not raised in the complaint filed in this proceeding, the Commission did not address this issue in its October 24 Order, and FPL Energy (nor any other party) previously raised this with the Commission. Significantly, no other party to this proceeding has had the opportunity to explore the evidence submitted in support of this new argument and we will reject FPL Energy's arguments in this regard. It is simply too late in this proceeding for FPL Energy to raise this matter.

19. FPL Energy also argues that the current method of reallocating excess recovery of revenue associated with the use of marginal losses is unjust and unreasonable as it distorts price signals to load. To solve this, FPL Energy submits an entirely new method for allocating loss revenues that it sets forth in the White Paper prepared by its consultant. Again, it is simply too late in this proceeding for FPL Energy to submit new evidence that no party has had an opportunity to examine. The proper forum in which FPL Energy should present new proposals is the ISO-NE stakeholder process or in a new complaint pursuant to section 206 of the FPA, in which all parties will have the opportunity to address the proposals and express any concerns they may have.

20. FPL Energy argues that the Commission should require ISO-NE to explain how it calculates the loss (or penalty) factor that it uses in calculating marginal losses. We disagree. As we stated in the October 24 Order, consistent with the Commission's "rule of reason," ISO-NE and NEPOOL provided sufficient specificity in its tariff in its Market Rule 1.²⁴ As we further pointed out in the October 24 Order, NEPOOL has provided on

²²*Baltimore Gas and Electric Co.*, 92 FERC ¶ 61,043 at 61,114 (2000) (citations omitted).

²³ *Southern California Edison Co.*, 102 FERC ¶ 61,256 at P 17 (2003).

²⁴ October 24 Order, 105 FERC ¶ 61,122 at P 21.

its website additional specificity, describing, among other things, the mathematical formula for calculating marginal losses. We find that ISO-NE and NEPOOL have provided sufficient specificity and transparency, and we see no reason to deviate from our existing "rule of reason" policy.

21. FPL Energy contends that the Commission erred in denying Northeast Utilities' complaint on the basis that Northeast Utilities did not show what the expected marginal loss costs were projected to be under the NE-SMD accepted by the Commission's September 20 Order. We find that the scale of the marginal losses that are recovered through LMP here are consistent with the Commission's objectives for the application of this rate design. The currently effective refund mechanism works exactly as it was designed to do – marginal losses in excess of actual losses are refunded to the NEPOOL Participants. As we explained, the existence of high marginal losses may be an indication of a high load on the transmission system, thereby indicating opportunities to investors and load and sending price signals.²⁵ We further stated that "[r]efunding excess loss revenues to the participants who incurred the losses would undermine the usefulness of including marginal losses in the LMP calculations." Refunding the excess LMP revenues to those who paid would result in those purchasers no longer paying the marginal cost for energy – the basic foundation of LMP.²⁶ As we stated, this outcome of LMP was known at the time the Commission accepted the use of marginal losses, it is consistent with Commission policy and it is within the levels the Commission expected. Parties' claims that marginal loss costs are greater than they expected does not make the methodology for marginal loss recovery unjust and unreasonable.

The Commission orders:

The requests for rehearing are hereby denied, as discussed in the body of the order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.

²⁵ *Id.* at P 19.

²⁶ *Id.* at P 20.